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In the Supreme Court of the United States

OCTOBER TERM, 1949

No. 745

JESSICA S. MAHANA, PETITIONER

v.

THE UNITED STATES

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINION BELOW

The opinion of the Court of Claims (R. 45-52) is reported in 88 F. Supp. 285.

JURISDICTION

The judgment of the court below was entered on February 6, 1950. (R. 52.) A motion for a new trial was overruled on April 3, 1950. (R. 52-53.) The petition for certiorari was filed on April 11, 1950. The jurisdiction of this Court is invoked under 28 U. S. C., Section 1255(1).

QUESTIONS PRESENTED

1. Whether Sections 22(k) and 171(a) of the Internal Revenue Code, which tax a divorced wife

on amounts received from her former husband, in certain circumstances, are constitutional.

2. If so, whether amounts paid by a divorced husband directly to his wife, in addition to income received by her from an alimony trust created by him, constitute periodic payments in discharge of a legal obligation imposed upon the husband under a written instrument incident to a divorce, within the meaning of Section 22(k) of the Code.

STATUTE AND REGULATIONS INVOLVED

The applicable provisions of the pertinent statute and Regulations are set forth in the Appendix, *infra,* pp. 12-19.

STATEMENT

The special findings of fact of the Court of Claims (R. 37-45) may be summarized as follows:

Petitioner was married to George S. Mahana in 1893, and they resided in New York State at all times material hereto. There were no children of the marriage. In 1922, petitioner and George separated and in the following year petitioner brought a suit against him for legal separation and separate maintenance. (R. 37.)

On November 12, 1923, after negotiations, petitioner and George entered into a permanent separation agreement under which he agreed to pay her $17,500 a year for the rest of her life "for her

separate maintenance and support and by way or in lieu of alimony." (R. 37.) The agreement provided that the husband would transfer certain securities in trust to the Guaranty Trust Company to secure the yearly payments and that if in any year the income from the trust was insufficient to make the stated payments of $17,500, the husband would pay the trustee a sum sufficient to make up the deficit; and that if in any year the income from the trust was less than $15,000, George would add additional securities to the trust if petitioner made demand therefor. This agreement also provided that petitioner and George each relinquished all claims on the other's property or estate and that it should in nowise prejudice any rights either of the parties had to institute suit for a divorce. (R. 38.)

On the same date George Mahana and the Guaranty Trust Company entered into an agreement whereby he delivered certain securities to the Trust Company under the same terms as those set forth in the agreement between George and his wife. (R. 38-39.)

On December 1, 1923, petitioner filed suit for an absolute divorce from her husband, and the divorce was granted on March 8, 1924. The decree became final November 6, 1924. No reference was made to alimony or support for the petitioner nor to the agreement of November 12, 1923, in the divorce decree. (R. 39.)

In 1929, disputes arose between George and petitioner involving the latter's federal and state income tax liability on the alimony payments which she had been receiving under the agreement of November 12, 1923. Petitioner contended that under the agreement $17,500 a year was to be paid to her net and free of all taxes, and that her interests were not protected under the agreement and the trust of November, 1923, especially in the event of George's death. (R. 39-40.) In March 1930, petitioner instituted an action in the Supreme Court of New York County to construe and enforce the provisions of the agreement and trust of November 12, 1923, asserting that it was the intent of the parties that George should pay all income taxes on the income received by her. This suit was settled and the terms of the settlement embodied in four letters from George dated June 28, 1933, one to the Guaranty Trust Company, and three to petitioner. These letters provided in substance that George would pay to the petitioner the amounts by which her state and federal income taxes were increased by reason of the receipt of $17,500 yearly, and that George would deposit additional securities with the trustee but that these securities should not become a part of the trust created in 1923. The income from these securities was to be used to supplement the income from the securities in the 1923 trust, but George reserved the power to sell or ex-

change the securities so deposited and substitute others therefor. (R. 40-42.)

During the taxable years 1943, 1944, and 1945, petitioner received $17,500 in each year from the Guaranty Trust Company consisting of income from the securities in the 1923 trust, income from the additional securities deposited by George in 1933, and amounts paid by George to the trustee necessary to make up the total of $17,500. In addition, George paid directly to petitioner $8,945.84 in 1943, $7,499.22 in 1944, and $3,730.03 in 1945, computed as the additional amount of United States and New York State income taxes petitioner had been required to pay by reason of her receipt of the alimony payments during each respective preceding year. (R. 42-43.)

In her income tax returns for each of the taxable years, petitioner reported the total amounts received from the trustee and from George in addition to her other income. She later filed timely claims for refund contending that none of the payments received from the Guaranty Trust Company or from George Mahana were taxable income to her. These claims were rejected, and suit was thereafter instituted in the Court of Claims. (R. 44.)

Upon the foregoing findings of fact the Court of Claims held that petitioner was taxable on the income so received and dismissed the petition. (R. 52.)

ARGUMENT

1. Section 22(k) of the Internal Revenue Code, as added by the Revenue Act of 1942 (Appendix, *infra*, pp. 12-14), provides that amounts received by a divorced wife in discharge of an obligation imposed upon her husband, because of the marital or family relationship, under the decree of divorce or under a written instrument incident to such divorce shall be included in the gross income of the wife. Section 171(a), added by the Revenue Act of 1942 (Appendix, *infra*, pp. 14-15), provides that there shall be included in the gross income of a wife who is divorced from her husband the amount of the income of any trust which she is entitled to receive and which would otherwise be includible in the gross income of her divorced husband. Provision is also made in Section 23(u) (Appendix, *infra*, p. 14), and Section 171(a) that such amounts shall be deducted from the husband's gross income.

The contention of the petitioner (Pet. 6-7) that these sections of the Code violate the Sixteenth Amendment[1] is without merit. Petitioner's princi-

[1] It is difficult to see how any tax could "violate" the Sixteenth Amendment. The plenary power to tax is found in Article I, Section 8 of the Constitution; that provision is "exhaustive and embraces every conceivable power of taxation." *Brushaber* v. *Union Pac. R. R.*, 240 U. S. 1, 12. The Sixteenth Amendment was adopted merely to make clear that the *source* of the income was immaterial and that a tax on income from property etc. was not to be regarded as the equivalent of a tax upon the property itself with the attendant requirement of apportionment, etc., as had been held in *Pollock* v. *Farmers' Loan & Trust Co.*, 157 U. S. 429, 158 U. S. 601.

pal reliance is on *Gould* v. *Gould,* 245 U. S. 151. But that case did not deal with Sections 22(k) and 171 of the Code or with the scope of the term "incomes" as used in the Sixteenth Amendment. It merely decided that the definition of "net income" contained in Section II A and B of the Revenue Act of 1913, c. 16, 38 Stat. 114, 166, was not intended to include monthly amounts paid to a legally separated wife for her support and maintenance. The *Gould* case in no way implies that Congress could not constitutionally provide, as it saw fit to do in Sections 22(k) and 171, that a divorced or legally separated wife's taxable income shall include alimony and support payments in certain circumstances. Similarly, the Court's rulings in *Douglas* v. *Willcuts,* 296 U. S. 1, *Helvering v. Fitch,* 309 U. S. 149, *Helvering* v. *Fuller,* 310 U. S. 69, *Helvering* v. *Leonard,* 310 U. S. 80, and *Pearce* v. *Commissioner,* 315 U. S. 543, go only to the construction of the particular tax statute involved. None of these cases implies that Congress lacks power under the Constitution to treat alimony payments as income taxable to the wife, and the *Pearce* opinion on the contrary expressly held the wife taxable on payments received from an alimony trust established by her husband. In any event, it is clear that the power to tax "incomes, from whatever source derived," under the Sixteenth Amendment includes the power to tax amounts received by divorced wives from their husbands di-

rectly and from trusts created, as to income, wholly or partly for their benefit, where such amounts are in no sense gifts but represent the discharge of obligations to the wife arising from the marriage contract. As the Court of Claims noted (R. 48), the amounts paid periodically to the wife are "income to spend, to live on, to save," and hence constitute "income to tax, if Congress sees fit, as it has, to tax it."

2. There is no conflict, as petitioner contends (Pet. 7-8), between the decision below and that of the Court of Appeals for the Second Circuit in *Commissioner* v. *Murray,* 174 F. 2d 816, and with those of the Court of Appeals for the Third Circuit in *Cox* v. *Commissioner,* 176 F. 2d 226, and *Brightbill* v. *Commissioner,* 178 F. 2d 404.[2] The *Murray* decision merely assumed without deciding that the language "incident to such divorce" in Section 22(k) means incident to the decree of divorce and not merely to the divorce. A similar assumption was made by the Court of Claims here. (R. 52.) The Third Circuit in the *Cox* case found it unnecessary

[2] Petitioner concedes that the income from the securities held in trust is taxable under Section 171, if that section is constitutional, but contends (Br. 21) that the amounts paid by the former husband to make good the deficits in trust income and the amounts paid to compensate her for taxes are not taxable under Section 22(k), since they were not periodic payments made under an agreement incident to a decree of divorce. Her position as to the amounts received from the additional securities deposited with the trustee in 1933 is not clear, so it is unnecessary to discuss it in view of the holding of the court below (R. 49-50) that they were a deposit in trust and are taxable under Section 171(a).

to determine the precise scope of the phrase "incident to such divorce," but held that the particular agreement there involved, made some eight months after the decree, was not incident to the divorce.

In *Commissioner* v. *Walsh,* decided April 24, 1950 (1950 C.C.H., par. 9277), the Court of Appeals for the District of Columbia Circuit, with Judge Edgerton dissenting, has held that the statutory language means incident to the decree of divorce. Since, as has been noted, the Court of Claims made a similar assumption as to the proper interpretation of the statute (R. 52) the two decisions do not conflict in this regard. Moreover, the holding in all of those cases that the written instruments were or were not "incident to such divorce" within the meaning of Section 22(k) turned on the particular facts involved, and thus do not give rise to any square conflict of decisions. However, it must be conceded that the construction made by the Court of Claims in this case differs, in its emphasis, from the construction placed upon the Section by the Court of Appeals for the District of Columbia Circuit. Since the problems involved are undoubtedly recurrent in nature, the Court may consider that a sufficient basis exists for review at this time.

However, this case did turn upon its facts, and in our view the facts fully warrant the conclusion of the Court of Claims that the 1923 and 1933 agreements, under which the trust income and the husband's additional payments were received by peti-

tioner, were incident to the decree of divorce. (R. 50-52.) The 1923 agreement was made only 13 days prior to the signing by petitioner of the complaint for divorce and at a time when she had pending a suit for legal separation and support (R. 50-51); the terms of the agreement show that it was made when divorce was contemplated and it was obviously the usual property settlement reached by the parties out of court in connection with the contemplated decree of divorce (R. 51). The 1933 agreement was not a new agreement but simply clarified the terms of the 1923 agreement (R. 51-52), and it therefore was also incident to the divorce (cf. R. 19-22, 40-41).

3. There is no merit to petitioner's contention (Br. 27) that the payments made by the husband under the 1933 agreement were not periodic. The term "periodic" is used in Section 22(k) to describe alimony payments required at intervals, "whether or not made at regular intervals," in contradistinction to a lump sum settlement and to installment payments discharging the principal sum of an obligation, stated in terms of money or property in the decree or written instrument, within a period of less than 10 years. The payments made, as required by the two agreements, by the husband in the taxable years, both to the trustee to augment the trust income so that $17,500 annually could be paid to the petitioner and to the

petitioner directly to reimburse her for income taxes incurred on the trust income, were made annually, were not in discharge of a lump or principal sum, and thus were clearly periodic payments under Section 22(k). It is sufficient that the agreements fixed the amounts to be paid by the husband annually in general terms, leaving the precise amounts in dollars to be determined by subsequent events. Cf. *Commissioner* v. *Murray,* 174 F. 2d 816 (C.A. 2d); *Lee* v. *Commissioner,* 10 T.C. 834; *Young* v. *Commissioner,* 10 T.C. 724. The petitioner does not assert a conflict on this point.

CONCLUSION

The decision below is correct in all respects and no square conflict of decisions is presented. The petition for certiorari should be denied.

Respectfully submitted,

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JUNE, 1950.

APPENDIX

Internal Revenue Code:

SEC. 22. GROSS INCOME.

(a) *General Definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service (including personal service as an officer or employee of a State, or any political subdivision thereof, or any agency or instrumentality of any one or more of the foregoing), of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *

(k) [as added by the Revenue Act of 1942, c. 619, 56 Stat. 798, Sec. 120(a)] *Alimony, etc. Income.*—In the case of a wife who is divorced or legally separated from her husband under a decree of divorce or of separate maintenance, periodic payments (whether or not made at regular intervals) received subsequent to such decree in discharge of, or attributable to property transferred (in trust or otherwise) in discharge of, a legal obligation which, because of the marital or family relationship, is imposed upon or incurred by such husband under such decree or under a written instrument incident to such divorce or sepa-

ration shall be includible in the gross income of such wife, and such amounts received as are attributable to property so transferred shall not be includible in the gross income of such husband. This subsection shall not apply to that part of any such periodic payment which the terms of the decree or written instrument fix, in terms of an amount of money or a portion of the payment, as a sum which is payable for the support of minor children of such husband. In case any such periodic payment is less than the amount specified in the decree or written instrument, for the purpose of applying the preceding sentence, such payment, to the extent of such sum payable for such support, shall be considered a payment for such support. Installment payments discharging a part of an obligation the principal sum of which is, in terms of money or property, specified in the decree or instrument shall not be considered periodic payments for the purposes of this subsection; except that an installment payment shall be considered a periodic payment for the purposes of this subsection if such principal sum, by the terms of the decree or instrument, may be or is to be paid within a period ending more than 10 years from the date of such decree or instrument, but only to the extent that such installment payment for the taxable year of the wife (or if more than one such installment payment for such taxable year is received during such taxable year, the aggregate of such installment payments) does not exceed 10 per centum of such principal sum. For the purposes of the preceding

sentence, the portion of a payment of the principal sum which is allocable to a period after the taxable year of the wife in which it is received shall be considered an installment payment for the taxable year in which it is received. * * *

(26 U.S.C. 1946 ed., Sec. 22.)

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

* * * * *

(u) [as added by the Revenue Act of 1942, *supra*, Sec. 120(b)] *Alimony, etc., Payments.*—In the case of a husband described in section 22(k), amounts includible under section 22(k) in the gross income of his wife, payment of which is made within the husband's taxable year. * * *

(26 U.S.C. 1946 ed., Sec. 23.)

SEC. 171 [as added by the Revenue Act of 1942, *supra*, Sec. 120(c)]. INCOME OF AN ESTATE OR TRUST IN CASE OF DIVORCE, ETC.

(a) *Inclusion in Gross Income.*—There shall be included in the gross income of a wife who is divorced or legally separated under a decree of divorce or of separate maintenance the amount of the income of any trust which such wife is entitled to receive and which, except for the provisions of this section, would be includible in the gross income of her husband, and such amount shall not, despite section 166,

section 167, or any other provision of this chapter, be includible in the gross income of such husband. * * *

(26 U. S. C. 1946 ed., Sec. 171.)

Treasury Regulations 111, promulgated under the Internal Revenue Code:

SEC. 29.22(k)-1. *Alimony and Separate Maintenance Payments—Income to Former Wife.*—(*a*) *In general.*—Section 22(k) provides rules for treatment in certain cases of payments in the nature of or in lieu of alimony or an allowance for support as between spouses who are divorced or legally separated under a court order or decree. For convenience, the payee spouse will hereafter in this section of the regulations be referred to as the "wife" and the spouse from whom she is divorced or legally separated as the "husband." See section 3797(a)(17).

In general, section 22(k) requires the inclusion in the gross income of the wife of periodic payments (whether or not made at regular intervals) received by her after the decree of divorce or of separate maintenance. Such periodic payments may be received from either of the two following sources:

(1) In discharge of a legal obligation which, because of the marital or family relationship, is imposed upon or incurred by the husband, or

(2) Attributable to property transferred (in trust or otherwise) in discharge of a

legal obligation which, because of the marital or family relationship, is imposed upon or incurred by the husband.

The obligation of the husband must be imposed upon him or assumed by him (or made specific) under either of the following:

(1) A court order or decree divorcing or legally separating the husband and wife, or

(2) A written instrument incident to such divorce or legal separation.

The periodic payments received by the wife attributable to property so transferred and includible in her income are not to be included in the gross income of the husband. See also section 29.171-1 in cases where such periodic payments are attributable to property held in trust.

The purpose and effect of section 22(k) may be illustrated, in general, by the following examples, in which it is assumed that the husband and wife make their income tax returns on the calendar year basis:

* * * * *

Example (*2*). W files suit for divorce from H. In consideration of W's promise to relinquish all marital rights and not to make public H's financial affairs, H makes a legally binding promise in writing to W to pay to her $200 a month if a final decree of divorce is granted without any provision for alimony. Accordingly, W does not request alimony and no pro-

vision for alimony is made under a final decree of divorce entered prior to 1942. During 1942, H pays W $200 a month, pursuant to the promise. The $2,400 thus received by W is includible in her gross income under the provisions of section 22(k). Under section 23(u), H is entitled to a deduction of $2,400 from his gross income.

* * * * *

(*b*) *Alimony income attributable to property.*—The full amount of periodic payments received under the circumstances described in section 22(k) is required to be included in the gross income of the recipient whether such amounts are derived, in whole or in part, from income received or accrued by the source to which such payments are attributable. Thus, it matters not that such payments are attributable to property in trust, to life insurance, endowment, or annuity contracts, or to any other interest in property, or are paid directly or indirectly by the obligor husband from his income or capital. For example, if in order to meet an alimony obligation of $500 a month, the husband purchases or assigns for the benefit of his former wife a commercial annuity contract paying such amount, the full $500 a month received by the wife is includible in her income, and no part of such amount is includible in the husband's income or deductible by him. See section 22(b)(2)(A) and section 29.22(b)(2)-4. Likewise, if property is transferred by the husband, subject to an annual charge of $5,000,

payable to his former wife in discharge of his alimony obligation under the divorce decree, the $5,000 received annually is, under section 22(k), includible in the wife's income, regardless of whether such amount is paid out of income or principal of the property.

The same rule applies to periodic payments attributable to property in trust. The full amount of periodic payments to which section 22(k) applies is includible in the wife's income, regardless of whether such payments are made out of trust income. This rule applies even though under the law applicable to taxable years beginning before January 1, 1942, only the income of a trust for the benefit of the divorced wife was taxable to her. Such periodic payments are to be included in the wife's income under section 22(k) and are to be excluded from the husband's income, even though the income of the trust would otherwise be includible in his income under section 22(a), section 166, section 167, or any other section of the Code or these regulations. As to periodic payments received by a former wife attributable to property in trust in cases to which section 22(k) does not apply because the husband's obligation is not specified in the decree or an instrument incident thereto, see section 171(a) and section 29.171-1.

* * * * *

(c) *Alimony installment payments.*—In general, installment payments discharging a part of an obligation the principal sum of which is, in terms of money or property speci-

fied in the decree of divorce or legal separation, or in an instrument incident thereto, are not considered "periodic payments" and therefore are not to be included under section 22(k) in the wife's income. An exception to this general rule is provided, however, in cases where such principal sum, by the terms of the decree or such instrument, may be or is to be paid within a period ending more than 10 years from the date of such decree or instrument. In such cases, the installment payment is considered a periodic payment for the purposes of section 22(k) but only to the extent that the installment payment, or sum of the installment payments, received during the wife's taxable year does not exceed 10 percent of the principal sum. This 10 percent limitation applies to installment payments made in advance but does not apply to delinquent installment payments for a prior taxable year of the wife made during her taxable year.

* * * * *

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